

**Before the
FEDERAL COMMUNICATIONS COMMISSION
WASHINGTON, D.C. 20554**

In the Matter of)	
)	
Annual Assessment of the Status of)	MB Docket No. 12-203
Competition in the Market for the)	
Delivery of Video Programming)	
)	

COMMENTS OF NETFLIX, INC.

Netflix, Inc. (“Netflix”) hereby submits these comments in response to the Commission’s Further Notice of Inquiry (“NOI”)¹ in the above-captioned proceeding.

When consumers decide to watch television today, they face a moment of truth: Will they pick up the remote and toggle through a linear grid of programs or will they decide to access content on demand, by clicking and watching? The on-demand category affords consumers new choices including a growing selection of Internet-delivered television shows and movies provided by Netflix, Amazon, Hulu, HBO GO, and other Internet competitors. These online video providers and other startups and device manufacturers are pushing incumbents to improve television user interfaces, including the increasingly archaic linear

¹ *Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, Notice of Inquiry, MB Docket No. 12-203, FCC 12-80 (rel. July 20, 2012) (“NOI”).

grid, to give consumers more choices in how and when they watch their favorite video programming.

Media, device, and delivery convergence means that content providers of all stripes are in a battle for consumer engagement. Before a consumer makes the decision to pick up a remote, that consumer has also made decisions about remote versus tablet, versus smartphone, versus a personal computer and the myriad options available on it, and more. Even after choosing which program to watch, consumers are increasingly engaging in “second screen” experiences.²

As discussed in more detail below, Netflix is working on a once-in-a-generation opportunity to transform the way consumers engage with video content. As the market continues to evolve, policymakers should ensure that incumbents do not use their dominance to stifle the innovation pioneered by Netflix and other new entrants.

I. NETFLIX CONTINUES TO TRANSFORM THE MARKET FOR VIDEO CONTENT DELIVERY

A. Netflix Continues to Grow

Netflix is the largest online video subscription service in the United States. Its U.S. subscribers alone now stream more than one billion hours per month of

² Second screen experiences bring together traditional TV shows and social media applications that consumers use on tablets, smart phones, or PCs while watching the show. See Jim Hanas, *The Race for the Second Screen: 5 Apps That Are Shaping Social TV*, Feb. 01, 2012, at <http://www.fastcocreate.com/1679561/the-race-for-the-second-screen-5-apps-that-are-shaping-social-tv>; see also Liz Shannon Miller, *Can Breaking Bad's Story Sync Get Viewers to Give Up Their DVRs*, Sep. 9, 2012, at <http://gigaom.com/video/can-breaking-bads-story-sync-get-viewers-to-give-up-their-dvrs/>.

movies and TV shows. In 2007, Netflix began offering consumers movies and TV shows streamed over the Internet to their PCs. Its online content library quickly grew, as did the number of Internet-connected devices upon which consumers could enjoy Netflix's streaming service. Today, consumers can access Netflix on more than 900 different Internet-connected devices. These devices include gaming consoles, an array of Blu-ray disc players, Internet-connected smart-TVs, home theatre systems, digital video recorders, Internet video players, mobile devices such as smartphones and tablets, and PCs.

With the increase in content and devices, so too came subscriber numbers. Today, Netflix has 24 million domestic streaming subscribers.³ Netflix offers consumers an unparalleled value proposition — for \$7.99 per month, subscribers can enjoy streaming all of the great movies and TV shows they want, whenever they want, and on whichever Internet-connected device they want.

Netflix's continued investment in technology and user interface design also works to enhance subscribers' viewing experience. Chief among those innovations is its catalog sorting algorithm, which makes content recommendations to a subscriber that are tailored to that subscriber's preferences.⁴ Through its recommendation engine, search capabilities, and social

³ Netflix also has 9 million DVD-by-mail subscribers; of those 9 million subscribers, almost 7 million also subscribe to the streaming service.

⁴ See Ben Fritz, *Cadre of Film Buffs Helps Netflix Viewers Sort Through the Clutter*, Sep. 3, 2012, at <http://www.latimes.com/entertainment/movies/moviesnow/la-fi-0903-ct-netflix-taggers-20120903,0,4683761.story>.

media features, Netflix endeavors to match subscribers with content they will love.

B. Netflix Continues to Expand Its Content Library, Including Original Programming

Netflix's continued expansion of its content catalog drives subscriber engagement measured by the number of hours subscribers spend watching movies and TV shows on Netflix. Among the popular TV shows that Netflix offers are *Mad Men*, *Breaking Bad*, *Gossip Girl*, *Pretty Little Liars*, and *The Lying Game*. Netflix has found that the availability of complete past seasons of currently on-air shows helps build the audience for new seasons of such shows.⁵ For example, newer seasons of shows such as *Mad Men*, *Breaking Bad*, *Sons of Anarchy*, and *The Walking Dead* have all seen significant viewership growth compared to past season increases after complete past season episodes were made available for streaming on Netflix.⁶ This phenomenon illustrates one of the ways in which Netflix is a complement to traditional linear TV providers. Netflix's role in the market also increases the pie for content providers seeking to

⁵ See Liz Shannon Miller, *Why Arrested Development on Netflix Could Change Everything*, Aug. 26, 2012, at <http://gigaom.com/video/why-arrested-development-on-netflix-could-change-everything/>.

⁶ See, e.g., Andy Fixmer, *'Mad Men' Premiere Draws Record Viewers on Netflix Boost*, Mar. 26, 2012, at <http://www.businessweek.com/news/2012-03-26/mad-men-premiere-viewership-rises-20-percent-on-boost-from-netflix>; Peter Kafka, *Netflix Affects TV Ratings – A Study*, Apr. 27, 2012, at <http://allthingsd.com/20120427/you-really-can-blame-the-web-for-shrinking-tv-ratings-but-you-have-to-credit-it-for-boosting-tv-too/>; Jeffrey Van Camp, *AMC says Netflix improved ratings for 'Mad Men' and 'The Walking Dead'*, May 11, 2012, at <http://www.digitaltrends.com/movies/amc-netflix-mad-men-the-walking-dead-ratings/#ixzz25dx7x3Pu>.

monetize their content. Netflix is having a similar market effect in other countries, such as in Canada.⁷

In addition to licensing content from studios and networks, Netflix is also beginning to invest in original programming.⁸ Netflix has four new shows under development: *House of Cards*, a political drama from acclaimed director David Fincher featuring actor Kevin Spacey; *Arrested Development*, the popular cult comedy that will return after being cancelled in 2006; *Orange is the New Black*; and *Hemlock Grove*. Additionally, Netflix expects to deliver a second season of *Lilyhammer*, the Norwegian drama that debuted on Netflix earlier this year. Netflix is continuing to explore opportunities to expand its lineup of original programming.

In addition to providing its subscribers with a wider array of programming to cater to individual preferences, Netflix's decision to invest in high quality original programming gives content producers an additional outlet for distributing their programming. By having the flexibility to deliver entire seasons of shows at once, or every day, or at other intervals — free of the traditional predefined weekly television time slots — Netflix also gives content

⁷ Canadian Radio-television and Telecommunications Commission, Communications Monitoring Report, September 2012, at 113, *available at* <http://www.crtc.gc.ca/eng/publications/reports/policymonitoring/2012/cmr2012.pdf> (data showing that Canadians who are Netflix subscribers watch more hours of television per week than Canadians who are not Netflix subscribers).

⁸ The Commission asked questions relating to OVDs producing or acquiring original programming. NOI at ¶ 68.

producers greater flexibility to structure storylines and produce shows.⁹ By allowing the show producers to more faithfully execute their artistic vision, Netflix is better able to satisfy consumer demand for innovative and high quality programming.

The growing quantity and range of content available via Netflix results in greater consumer satisfaction and more word-of-mouth referrals, leading to more subscribers and revenue, which in turn allows Netflix to invest in new content — feeding the virtuous cycle of growth.

II. NETFLIX'S PLACE IN THE VIDEO PROGRAMMING MARKET IS SIMILAR TO A CABLE CHANNEL

In the *NOI* and in earlier proceedings, the Commission has asked or examined the question of whether OVDs compete with MVPDs.¹⁰ Netflix has previously explained that it is a complement to, rather than a substitute for, MVPD service.¹¹ The overwhelming majority of Netflix subscribers continue to rely on MVPDs for news, live sports, current season shows on cable networks, and other entertainment. Netflix's continued growth and evolution have confirmed this conclusion, and indeed has clarified that Netflix more closely

⁹ See Liz Shannon Miller, *Why Arrested Development on Netflix Could Change Everything*, Aug. 26, 2012, at <http://gigaom.com/video/why-arrested-development-on-netflix-could-change-everything/>.

¹⁰ *NOI* at ¶ 60; see also *Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, Further Notice of Inquiry, MB Docket No. 07-269, FCC 11-65, at 5 n.16 (rel. Apr. 21, 2011); *Application of Comcast Corporation, General Electric Company and NBC Universal, Inc. for Consent to Assign Licenses and Transfer Control of Licenses*, Memorandum Opinion and Order, MB Docket No. 10-56, FCC 11-4, at ¶¶79-85 (rel. Jan. 20, 2011).

¹¹ Comments of Netflix, Inc., MB Docket No. 07-269, at 4-5 (June 8, 2011).

resembles cable channels such as HBO rather than a substitute for an entire MVPD service.

Given its mix of original programming and other content, and its pricing, Netflix is positioned in the market similar to HBO and other other arrivals in the streaming market, such as Amazon, that supplement rather than replace a cable package that includes hundreds of channels and costs approximately 10 times the cost of a Netflix subscription.

When policymakers examine competition faced by MVPDs, the presence of an OVD such as Netflix should not be overstated. With no live news or sports programming, Netflix does not offer a complete substitute for MVPDs. Accordingly, the presence of online video providers such as Netflix will not necessarily discipline price increases for the complete bundle of MVPD video programming.

III. NETFLIX IS INVESTING IN ITS OWN CONTENT DELIVERY NETWORK TO PROVIDE BETTER SERVICE TO CONSUMERS

As mentioned above, Netflix subscribers currently enjoy over a billion hours of programming every month. As traffic from Netflix and other OVDs has grown, ISPs have responded by, among other things, introducing tiered pricing and/or data caps,¹² and seeking to impose charges for the delivery of Internet

¹² See Brian Stelter, *Sweeping Effects as Broadband Moves to Meters*, June 26, 2012, at <http://www.nytimes.com/2012/06/27/business/media/internet-providers-testing-metered-plans-for-broadband.html>; Lawrence LeBlond, *Broadband Data Caps Scrutinized by Internet Companies, Lawmakers*, June 28, 2012, at <http://www.redorbit.com/news/technology/1112647503/broadband-data-caps->

traffic.¹³ For its part, Netflix has introduced its own content delivery network (“CDN”), called Open Connect, to more efficiently deliver Netflix traffic at no cost to the locations the ISP desires.¹⁴ ISPs can also choose to receive Netflix data at common internet exchanges. To assist ISPs, Netflix has shared its hardware design and the open source software components of the Open Connect server.

These cost-efficient designs will lead to a faster, less expensive Internet for all, and is an example of steps that edge-based providers of content and applications can take to play a role in optimizing the usefulness and speed of broadband networks. Too often, broadband delivery improvements are seen as exclusively under the control of ISPs, and the only way to address traffic management is via techniques such as tiered pricing. Through options such as Open Connect, Netflix and other edge-based content providers such as YouTube have shown that there are other, more consumer-friendly approaches to addressing the growth of broadband traffic.

However, to realize the benefits of Netflix’s Open Connect program, incumbent broadband network operators must interconnect their access

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¹³ The issue of imposing charges for the delivery of Internet traffic was central to a dispute between Comcast and Level 3 that began in 2010. *See, e.g., Ex Parte* Letter from John M. Ryan, Assistant Chief Legal Officer, Level 3 Communications, Inc. to Marlene H. Dortch, Secretary, FCC, GN Docket No. 09-191, WC Docket Nos. 07-52 & 10-127 (Dec. 10, 2010); *Ex Parte* Letter from John M. Ryan, Chief Legal Officer, Level 3 Communications, Inc. to Marlene H. Dortch, Secretary, FCC, GN Docket No. 09-191 (Jan. 14, 2011).

¹⁴ Ken Florance, Vice President of Content Delivery, Netflix, Inc., *Announcing the Netflix Open Connect Network*, June 4, 2012, at <http://blog.netflix.com/2012/06/announcing-netflix-open-connect-network.html>.

networks with Open Connect servers. If Tier 1 operators refuse to interconnect with Open Connect, they will have made a decision to forgo a more efficient, cost-effective method for delivering video via the Internet. Policymakers should not allow incumbent broadband network operators to stifle innovative traffic delivery methods, particularly when incumbent operators are complaining about capacity constraints.¹⁵

IV. CONCLUSION

As the Commission continues to examine the market for the delivery of video programming and the role of OVDs in providing increasing options to consumers, Netflix urges the Commission to remain mindful of the threats to OVDs and be prepared to take action to protect consumers if necessary. As explained above, Netflix is not a substitute for MVPD service. Nevertheless, Netflix and other Internet video start-ups provide consumers with additional choices and new outlets for video programming, and it is in the public interest for the Commission to preserve such consumer choice.

As Netflix has explained in the past,¹⁶ given that OVDs are reliant on ISPs

¹⁵ See Cathy Avgiris, Executive Vice President and General Manager, Communications and Data Services, Comcast Cable, *Comcast to Replace Usage Cap With Improved Data Usage Management Approaches*, May 17, 2012, at <http://blog.comcast.com/2012/05/comcast-to-replace-usage-cap-with-improved-data-usage-management-approaches.html> (justifying data caps and tiered pricing for individual users by citing capacity constraints); Joint Opposition to Petitions to Deny and Comments by Cellco Partnership d/b/a Verizon Wireless et al., WT Docket No. 12-4, at 12-23 (Mar. 2, 2012) (discussing capacity constraints on Verizon Wireless's network).

¹⁶ See Comments of Netflix, Inc., MB Docket No. 07-269, at 5-8 (June 8, 2011).

to deliver their services and that ISPs and MVPDs are typically the same entities, OVDs face threats because of the market power of network operators. Netflix continues to face threats from ISPs in the following ways:

(1) ISPs can favor their own traffic, either by prioritizing their own bits or by not counting their own or affiliated bits toward data caps imposed by the ISP.

(2) ISPs can either refuse, or charge Netflix for, sufficient entry ports to their networks to deliver the Netflix video traffic that Netflix subscribers have requested, even though these subscribers have paid for their broadband connections from the ISP.

(3) ISPs can impose usage based billing or data caps, even though off-peak usage has zero marginal cost and does not impact network congestion.¹⁷

Netflix urges the Commission to remain vigilant of such threats and to take steps if needed to protect consumer choice by preserving the additional outlets for video programming.

¹⁷ See *id.* at 8.

Respectfully submitted,

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